

# Affairs of the Heart

## A Peek at the Czech Republic

by William Corley

*Export America*

The Czech Republic, the midpoint of Europe, has emerged from four decades of Communist rule and more than a decade of economic and political reform to regain a preeminent role in Central Europe. Located at the crossroads of ancient trade routes and modern information highways, the capital city of Prague welcomes U.S. investors and exporters to a country that has not forgotten its democratic, free-market traditions.

### STABILITY AND GROWTH

The transformation of the Czech Republic since the Czechoslovak “velvet revolution” in November 1989 and “velvet divorce” in January 1993 has been impressive. In 1991, on the eve of large-scale privatization, state-owned industry generated more than 90 percent of Czech GDP. Twelve years later, on the eve of accession to the European Union, the private sector dominates economic activity.

The Czech Republic has strung together several years of solid economic growth and accumulated foreign direct investment worth billions of dollars. Its economy experienced recession in the late 1990s, but even in recovery, GDP growth has averaged more than 2.5 percent in the last two years, meaning the Czech economy has outperformed the major advanced economies of the world. While unemployment is currently high, a recent

### FACTS AND FIGURES

**Total area:** 78,866 square km (a little smaller than South Carolina)

**Population:** 10.3 million

**GDP:** \$91 billion (2003 forecast)

**GDP by sector:** services 55%, industry 41%, agriculture 4%

**Main industries:** metallurgy, machinery and equipment, motor vehicles, glass, armaments

**Exports:** machinery and transportation equipment, intermediate manufactures, chemicals, raw materials, fuel

**Imports:** machinery and transportation equipment, intermediate manufactures, raw materials, fuels, chemicals

Sources: CIA, EIU.

EBRD forecast puts 2003 economic growth at 3 percent, with inflation at an annual rate of 1.3 percent. Such performance places the Czech Republic slightly below the EBRD average GDP growth forecast for Central and Eastern Europe, but much higher than that for the European Union. The Czech Ministry of Finance, noting the weak growth of the euro zone and in particular Germany, the largest trading partner of the Czech Republic, is less optimistic but still expects GDP growth of 2.3 percent this year and 3 percent in 2004.

### THE HEART OF EUROPE

The Czech Republic has meanwhile rejoined Central Europe. Whereas the former Czechoslovakia spent the Cold War in Soviet-dominated “Eastern Europe,” the Czech Republic and its neighbors are now in “Central Europe.” Part of an old joke goes that Stalin placed Prague in Eastern Europe, despite the city being both north and west of Vienna, Austria, which was considered part of Western Europe during the Cold War. The

humor is bittersweet, but the Czechs have the last laugh, since the country is geographically and culturally Central European. Appropriately, Prague is home to Charles University, the oldest university in Central Europe (established in 1348).

The Czech Republic has realigned its economic relations and foreign affairs with Western and Central Europe. Since 1993, Czech exports have boomed, with most now going to the European Union (which supplies two-thirds of imports). Exports make up more than 60 percent of Czech GDP. Meanwhile, the Czech Republic has become a WTO, OECD, and NATO member. The country is scheduled to become an EU member in May 2004.

### MARKET PERSPECTIVES

The Czech Republic, despite its Soviet bloc antecedents, is a sophisticated marketplace. Its significant progress in moving from a socialist system to a capitalist market reflects the democratic and commercial traditions of the first Czechoslovak



Republic, from 1918 to 1938. (Older generations have not forgotten that interwar Czechoslovakia was more industrialized than Austria and one of the wealthiest nations in Central Europe.) Yet it is somewhere in this mix of strong tradition, socialist hang-over, and emerging-market capitalism that the Czech commercial climate is perhaps best understood.

The Czechs are hardworking, well-educated people. On average, Czechs work more hours (nearly 2,000) annually than Americans, Japanese, Britons, Swiss, and Germans. Czechs are quite productive, as measured in GDP per hour of work. They are less productive than Western Europeans and Americans, but more productive than South Koreans, Mexicans, and Poles, and the Czech Republic ranks just outside the top 20 productive nations in the world, according to the Conference Board. Meanwhile, elementary school attendance in the country is approximately 90 percent, according to UNICEF, a figure that is higher than that of Germany (long considered a nation of extremely high educational standards). OECD studies of literacy of youth as well as educational attainment of adults rank the Czech Republic well above the OECD average, and particularly high in scientific literacy of 15-year-old students. Political and societal norms tend toward the progressive and modern. For instance, women hold nearly a fifth of parliamentary seats, which translates into significantly more

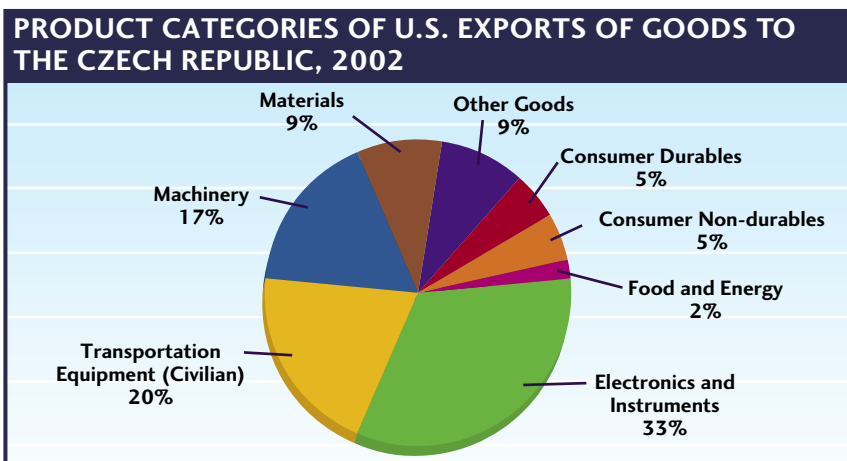
female participation in a federal representative assembly than in the United States, France, and Italy.

The Czech Republic is modern if not cutting-edge in other ways as well. Interestingly, the number of telephone lines per 1,000 inhabitants is under 400, a low figure in comparison with wealthy and industrialized Western European nations. This is due in part to the old fixed-line system, which entailed poor service and long waits for installation of new lines. However, Czechs have rapidly adopted new technologies. The cellular phone penetration rate is 80 percent, which is higher than that of Western Europe, according to *Global Mobile*. (Cellular penetration in the United States is about 50 percent.) Annual mobile-phone subscription growth is more than 35 percent, compared with less than 10 percent in Western Europe. Internet usage (perhaps 15 percent of the

population) is also relatively high in the Czech Republic in comparison with its Central-Eastern European neighbors and in view of the country's transition to capitalism. While Internet usage is well below the Western European average, it is comparable with that of Spain and Greece, two EU members since the 1980s. The Czech Republic spends approximately 4 percent of GDP on information technology, which is comparable with the EU average and much higher than that of neighboring countries of the former Soviet bloc.

Comparisons with Western Europe and the European Union in particular invariably raise the issue of the relative wealth of the Czech Republic. The Economist Intelligence Unit, in a forecast for 2003, calculates Czech GDP per capita at \$8,880 (which would make the Czech Republic wealthier than any other former Communist country in Central-Eastern Europe, except Slovenia with \$11,370 GDP per capita). However, Austria and Germany, the "Western" neighbors of the Czech Republic, both boast GDP per capita of just over \$29,000. (U.S. GDP per capita is estimated at \$37,000.)

Using 2000 data at purchasing-power parity, the World Bank sets Czech GDP per capita at \$13,780. By comparison, the EU average according to the same World Bank purchasing-power calculations is \$23,550, with the GDP



per capita of EU accession candidates Malta and Slovenia at \$16,530 and \$17,310, respectively, and that of EU members Portugal and Greece falling in between. Nevertheless, Czech GDP per capita, at 2002 purchasing-power parity, is only two-thirds of the 30-nation OECD average.

The silver lining to relative wages and living standards is that the Czech Republic is already a stable market for foreign consumer goods, a low-cost manufacturing base, and a gateway to both the European Union and Central-Eastern Europe. Further, EU accession is expected to accelerate economic growth and institutional change.

Wealthy or not, the Czech Republic is developing free-market institutions. Privatization, as noted, has transformed the Czech economy. Reform and restructuring continues in key industrial sectors, including telecommunications, energy, and transportation infrastructure. Change has not always been easy, but the country has taken on the challenges of harmonizing its laws, regulations, and standards with those of the European Union, all in preparation for pending accession.

"Right now could be a good time to for U.S. companies to enter the Czech market, develop strong relationships, and thus have brand recognition and market share before accession," says Anthony Hemstad, founder



Prague neighborhood with castle area in background.

and regional director of Eklektik Communications, a full-service public relations/affairs agency headquartered in Prague. "The Czech Republic is a low-crime, physically safe environment, and the laws are improving," explains Hemstad, an American who has done business in Prague since 1991. "You still need a good contract, good local lawyers, and adjudication preferably outside the country."

#### TRENDS AND OPPORTUNITIES

As the Czech economy has developed internally and expanded internationally, many commercial opportunities have arisen for foreign companies. Among emerging markets in Central and Eastern Europe, the Czech Republic is the most popular investment location, as measured by foreign direct investment per capita. The majority of foreign direct investment comes from the European Union. By country, the United States is the fifth-largest investor in the Czech Republic, according to the Czech National Bank, with \$2.5 billion of cumulative investment, 1993–2002. Key areas of foreign investment in the Czech Republic include transportation,

storage, and communications; financial intermediation; trade, hotels, and restaurants; machinery and equipment manufacturing; and real estate and other business services.

The U.S. Commercial Service contends that American companies will continue to profit from the ongoing transformation of the Czech economy, including upgrading of telecommunications equipment and services, pollution control equipment, energy production and distribution, housing, municipal infrastructure, and medical services. Continued privatization, particularly in transportation and energy sectors, should present several trade and investment opportunities for U.S. firms.

The latest *Country Commercial Guide* for the Czech Republic describes the top prospects for U.S. businesses in several sectors. Telecommunications is a particularly strong market, and U.S. exporters may find lucrative opportunities in the provision of network and wireless equipment, data and voice services, videoconferencing equipment, video telephones, and faxes.

#### LEADING SECTORS FOR U.S. EXPORTS AND INVESTMENT

- Automotive parts, services, and equipment
- Financial services
- Manufacturing machinery
- Pollution control equipment and services
- Telecommunications equipment and services
- Security and safety equipment and services

Source: *Country Commercial Guide: The Czech Republic*, FY 2003.



Exporters of environmental technology may also wish to consider the Czech Republic. Like other countries in Central-Eastern Europe, the republic faces the task of adopting strict environmental standards in order to join the European Union.

The Czech government has invested heavily in the environment and infrastructure to make the country eligible for EU accession. The total cost of meeting EU environmental standards may run to several billion dollars, of which water and wastewater treatment could take more than one-third of investment. Conforming to EU standards for waste handling may cost several hundred million dollars and include biodegradable waste treatment, packaging, waste recycling, and used tire disposal.

Tourism, while significantly depressed by global recession, is another interesting sector. Czechs continue to spend a higher proportion of their incomes on vacations, and the high end of the tourism market has seen a wave of luxury cruises, ski trips, and overseas golf tours. Mag Consulting says that Czechs spent an average of 14,937 crowns (approximately \$538 at the current exchange rate) on vacations in 2001, compared with 13,998 crowns (\$503) in 2000. However, economical family holidays in the Czech Republic and nearby Slovakia have become increasingly popular among Czechs, and several local tourist agencies took to the Internet in the late 1990s to rent cottages in the countryside.

Given the growth of Internet usage and overall Internet sales (which exceed \$70 million annually in the Czech

Republic), U.S. travel and tourism providers may find lucrative opportunities in the Czech market. Prague dominates the Czech tourism industry and attracts more than three-quarters of all foreign visitors. According to most industry analysts, the Czech hotel market is saturated, although there may be still be some opportunities in small-scale accommodations and mid-range hotels. Additional prospects, according to the U.S. Commercial Service, include ticketing and reservation services, hotel management, amusement parks, golf courses, and sight-seeing tours.

U.S. companies interested in the Czech Republic should do their homework. "One of the biggest mistakes that small and medium-sized exporters to the Czech Republic make is that they don't do proper product tests to determine market demand and cultural fit," says Joel Ranck of Lincoln Park Communications, a Washington, D.C., firm with extensive ties to and experience in the Czech Republic.

The Czech Republic welcomes U.S. products and services. As EU accession approaches (pending a Czech referendum in mid-June 2003), the timing is right for U.S. businesses to consider the promising future of the heart of Europe.

This article drew from several sources, including among others the Czech National Bank, Organization for Economic Cooperation and Development, CzechInvest, *Country Commercial Guide: Czech Republic, FY 2003* (U.S. Commercial Service and U.S. Department of State, 2002), *The World in 2003* (The Economist Newspaper Ltd., 2002), *The World Factbook* (CIA, 2002), *Prague Business Journal*, and *Financial Times*. U.S. export statistics compiled by Howard Schreier, ITA Office of Trade and Economic Analysis (U.S. Census Bureau data; product categories based on end-use classification).

#### REALITY CHECK

- Strategic location
- EU accession prospects
- Stable and relatively prosperous
- Bureaucracy and corruption hinder commerce
- Kafkaesque legal system requires patience
- U.S. products well regarded
- More formal dress and manners than American business
- Democratic, free-market traditions
- Continued reform and bright future





## CZECH NATIONAL HOLIDAYS

**January 1**

New Year's Day and Establishment Day (founding of the Czech Republic, 1993)

**(Varies by Year)**

Easter Monday

**May 1**

Labor Day

**May 8**

Liberation Day (end of World War II)

**July 5**

Cyril and Methodius Day (for the Christian missionaries of the ninth century A.D.)

**July 6**

Jan Hus Day (for the religious reformer and martyr)

**September 28**

St. Wenceslas Day (for the patron saint of the Czech nation)

**October 28**

Statehood Day (founding of Czechoslovakia, 1918)

**November 17**

Freedom and Democracy Day (for anti-Nazi demonstrations in 1939 and anti-Communist demonstrations in 1989)

**December 24**

Christmas Eve

**December 25 and 26**

Christmas Holidays

Source: Embassy of the Czech Republic, Washington, D.C.

## WEB RESOURCES

**Central and Eastern Europe****Business Information Center**

This U.S. Commerce Department office offers extensive information about the Czech Republic and its neighbors, including export tips, trade leads, economic figures, and more. The site also has the latest *Country Commercial Guide* and several other resources.

[www.export.gov/ceeibic](http://www.export.gov/ceeibic)

**U.S. Commercial Service Market Research**

This site offers a wide range of country and industry information. The Market Research Report link provides access to the *Country Commercial Guide* and other information about business in the Czech Republic.

[www.export.gov/marketresearch.html](http://www.export.gov/marketresearch.html)

**U.S. Commercial Service in the Czech Republic**

The Commercial Service operates out of the U.S. embassy in Prague. This site provides an introduction to Commercial Service programs, including links to [www.buyusa.gov/czechrepublic/en](http://www.buyusa.gov/czechrepublic/en) and its on-line trade promotion offerings.

<http://prague.usembassy.gov/fcs/fcs.htm>

**American Chamber of Commerce in the Czech Republic**

This independent association of businesses promotes commercial relations between the Czech Republic and the United States. Its activities include seminars, briefings, and other educational and networking events that facilitate doing business in the Czech Republic.

[www.amcham.cz](http://www.amcham.cz)

**Embassy of the Czech Republic in Washington, D.C.**

This site contains a wealth of links, such as a trade directory, a "doing business in" guide, and historical/cultural facts.

[www.mzv.cz/washington](http://www.mzv.cz/washington)

**CzechInvest**

The Czech Ministry of Industry and Trade operates the CzechInvest agency to promote foreign direct investment in the Czech Republic. This site explains the advantages of investing in the country, describes key manufacturing and services sectors, and charts foreign investment by industry and region. CzechInvest services range from initial contact facilitation to post-investment consulting, available through several branch offices, including the Midwest (Chicago) and Silicon Valley (Campbell, Calif.).

[www.czechinvest.org](http://www.czechinvest.org)

**Periodicals in English about the Czech Republic**

*Prague Business Journal* ([www.pbj.cz](http://www.pbj.cz)), a weekly, and *The Prague Tribune* ([www.prague-tribune.cz](http://www.prague-tribune.cz)), a monthly, both provide trade and investment news and free e-mail newsletters. *The Fleet Sheet* is a daily roundup of business and political news in the Czech Republic, and its Web site ([www.fleet.cz](http://www.fleet.cz)) offers a free daily e-mail bulletin. *The Prague Post* ([www.praguepost.com](http://www.praguepost.com)), a weekly newspaper, also covers business and offers an e-weekly.